

**DEPARTMENT OF STATE REVENUE  
LETTER OF FINDINGS NUMBER: 07-0445  
Gross Income Tax  
For Tax Year 2002**

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**ISSUE**

**I. Gross Income Tax—Partnerships.**

**Authority:** IC § 6-2.1-3-25 (repealed 2003); IC § 6-3-1-10; IC § 6-3-1-19; I.R.C. § 7704; Treas. Reg. § 301.7701-2 (as amended in 2007).

Taxpayer protests the assessment of gross income tax with respect to receipts earned by a limited partnership taxed as a corporation for federal income tax purposes.

**STATEMENT OF FACTS**

Taxpayer is a corporation. Taxpayer owned two single-member limited liability companies, LLC 1 and LLC 2. LLC 1 owned a one percent general partnership interest and LLC 2 owned a ninety-nine percent limited partnership interest in Partnership. Partnership operated Taxpayer's retail locations in Indiana. For tax purposes, LLC 1 and Partnership are treated as corporations.

During the year in question, Taxpayer did not report the entire Indiana gross receipts from Partnership as gross income for gross income tax purposes. The Department assessed Taxpayer, and in the alternative Partnership, with gross income tax based on Partnership's total Indiana gross receipts. Taxpayer protested the assessment, and this Letter of Findings results.

**I. Gross Income Tax—Partnerships.**

**DISCUSSION**

Taxpayer protests that Partnership should be treated as a tax-exempt partnership for gross income tax. In particular, Taxpayer protests that Partnership is treated as a partnership regardless of whether Partnership is a disregarded entity or is taxable as a corporation for federal tax purposes.

IC § 6-2.1-3-25 (repealed 2003) provided:

- (a) As used in this section, “partnership” and “partner” have the same meanings as those terms are defined in IC 6-3-1-19.
- (b) Gross income received by a partnership is exempt from gross income tax. However, gross income is not exempt from the gross income tax if it is received by a publicly traded partnership that is treated as a corporation for federal income tax purposes under Section 7704 of the Internal Revenue Code.

IC § 6-3-1-19 provides:

- (a) The term “partnership” includes a syndicate, group, pool, joint venture, or other unincorporated organization through or by means of which any business, financial operation, or venture is carried on, and which is not, within the meaning of this chapter, a corporation or a trust or an estate. The term also includes a limited liability company that is treated as a partnership for federal income tax purposes.
- (b) The term “partner” means a member of a partnership.

Partnership is not a trust or an estate. However, Partnership elected treatment as a corporation for federal tax purpose. For Indiana tax purposes, “corporation” is defined by IC § 6-3-1-10, which states:

The term “corporation” includes all corporations, associations, real estate investment trusts (as defined in the Internal Revenue Code), joint stock companies, whether organized for profit or not-for-profit, any receiver, trustee or conservator thereof, business trusts, Massachusetts trusts, any proprietorship or partnership taxable under Section 1361 of the Internal Revenue Code, and any publicly traded partnership that is treated as a corporation for federal income tax purposes

Partnership does not meet the definitions of corporation contained in IC § 6-3-1-10. The closest provision under the corporate income tax section, a “proprietorship or partnership taxable under Section 1361 of the Internal Revenue Code,” pertains to a section of the Internal Revenue Code that permitted certain entities to elect corporate status for federal tax purposes; however, the section as it was then written was no longer effective as of 1969.

Treas. Reg. § 301.7701-2(a) (as amended in 2007) states:

Business entities. For purposes of this section and § 301.7701-3, a business entity is any entity recognized for federal tax purposes (including an entity with a single owner that may be disregarded as an entity separate from its owner under § 301.7701-3) that is not properly classified as a trust under § 301.7701-4 or otherwise subject to special treatment under the Internal Revenue Code. A business entity with two or more members is classified for federal tax purposes as either a corporation or a partnership. **A business entity with only one owner is classified as a corporation or is disregarded; if the entity is disregarded, its activities are treated in the same manner as a sole**

**proprietorship, branch, or division of the owner.** But see paragraphs (c)(2)(iv) and (v) of this section for special employment and excise tax rules that apply to an eligible entity that is otherwise disregarded as an entity separate from its owner. **(Emphasis added)**

The effective result of Taxpayer's argument is that Partnership is able to claim the benefits of corporate status for federal tax purposes and Indiana adjusted gross income tax advantages. However, for Indiana gross income tax purposes, Taxpayer argues that it can rely on Partnership's legal status as a limited partnership for Partnership to be taxed as a partnership (i.e., its partners or the ultimate taxable entity are taxable on the partnership's distributive share of net earnings rather than the partnership's receipts). Thus, Taxpayer argues that it can seek the tax advantages of its inconsistent statuses for both federal and state law. Due to the interplay of federal income tax and Indiana gross income tax laws, Taxpayer is permitted this result with respect to Partnership.

A partnership must have two or more partners; otherwise the partnership is either disregarded or treated as a corporation for federal tax purposes. LLC 1 and Partnership are treated as corporations; LLC 2 is a disregarded entity.

However, gross income tax does not incorporate the federal definition of a business entity. Partnerships and corporations have different gross income tax definitions than their respective federal tax definitions. Thus, the federal tax treatment of Partnership—a corporation—does not necessarily equate to its Indiana tax treatment.

Furthermore, the Department has issued several revenue rulings with respect to what constitutes a partnership for gross income tax purposes. Two themes are consistent through the revenue rulings. One theme is that a partnership is still respected as a partnership for gross income tax purposes even if the partnership is disregarded for federal tax purposes. The second theme is that a partnership is only taxed as a corporation if it is a publicly traded partnership as defined by I.R.C. § 7704.

Partnership was a partnership for gross income tax purposes even though it could only be defined as a disregarded entity or a corporation for federal income tax purposes. As such, Taxpayer's treatment of Partnership's gross receipts was proper, and Taxpayer's protest is sustained.

### **FINDING**

Taxpayer's protest is sustained.